HIGH FOOD PRICES, MIDDLEMEN, AND SPECULATION

BY L. D. H. WELD

PRICES of foods, which have been rising since 1896, had reached such a high point even before the European War, that they were causing general anxiety and unrest. But since the war began, they have mounted upward to unprecedented heights,—not so much during 1914 and 1915,—but more especially during the latter half of 1916 and the first part of 1917. The possibility of serious food shortage, and the activities of the Government with regard to food production and distribution, have accentuated the interest in the present abnormal prices.

One point that is often lost sight of in discussing price increases is the fact that the prices of all foodstuffs have not risen uniformly; some have risen abnormally, whereas others have remained practically stationary. On February 15th, 1917, for example, the price of potatoes was 88 per cent. higher than the average monthly price of 1916; beans had risen 35 per cent.; eggs, 35 per cent.; and onions, 149 per cent. On the other hand, round steak had risen only 6 per cent.; bread, 9 per cent.; prunes, 5 per cent.; and rice, tea and coffee had not risen at all. Many other important commodities had risen but moderately. There have been many changes in prices since February, and the crops of 1917 have now become a dominant factor; but it is the price situation of the early part of 1917 with which this discussion deals.

High prices are a hardship only if they have risen faster than wages. It is well known that wages have been advancing rapidly during the past few months,—but not so rapidly as prices. That is the usual rule,—wages lag behind prices. Although wages have not gone up as rapidly as the prices of potatoes, onions, beans, and eggs, they have undoubtedly gone up faster than the prices of meats, rice, prunes, tea,

coffee, and many other commodities. Therefore, the power of substituting one commodity for another, the cheaper for the dearer, at least alleviates the situation. Add to this the fact that there has been steady employment for any man (or woman) with half a mind and half a body, and it is no wonder that investigations on the Lower East Side in New York have revealed the fact that there is no more suffering among the poor classes than usual. In other words, there was not much real economic excuse for the so-called "food riots," which were at least partly due to an inability of certain foreign elements to adapt their diets from potatoes, onions, etc., to other foods which are low in price and sufficiently nutritious.

The reasons for the recent increase in prices are not hard to locate; in fact, the principal causes are perfectly obvious to anyone who really studies conditions and statistics. They may be enumerated as follows: first, short crops; second, unusual demand; and third, a large increase in the money supply. Many people consider food speculation as one of the causes, but we shall come back to that later.

Taking these three causes up in reverse order, the money supply of the country has been augmented largely as a result of the great influx of gold which has been sent to us in payment for our exports. An increasing supply of money has the effect of lowering the purchasing power of the dollar, which in turn means that prices are higher. An increasing volume of trade, which calls for a greater amount of money in order to carry on business, may offset this tendency, and since we have been enjoying such an increase in trade activity, it is impossible to say just how much effect the increase in money supply has had on prices; but it has at least been an important factor.

The unusual demand for commodities occasioned by the European War has been in two ways: first, by causing foreign nations to enter our markets to buy foodstuffs for export; and second, by stimulating our manufacturing industries to such an extent as to create an unprecedented period of prosperity. Foreign buying of foodstuffs has not been as important a factor as most people think, except in the case of grains and meats. The exports of potatoes and many other high-priced products have been infinitesimal, although even small exports have their effect on prices. But the unprecedented prosperity has resulted in a huge domes-

tic demand, because of steady employment and high wages. In other words, people in general are demanding and buying more commodities than ever before. This is a conspicuous reason for high prices today.

But the most important and obvious reason is short crops. This would furnish a sufficient explanation, if there were no other factors making for high prices; fortunately this factor is easily measurable by means of Government statistics. The year 1915 was our banner year in crop production, and therefore prices stayed down through the winter and spring of 1915-16. Nineteen-sixteen was the poorest crop year we had had for several years. The acreage planted in 1916 did not differ materially from that of 1915, but because of unusually adverse climatic conditions, there was a reduced output per acre. In fact, during the last sixteen years, there has been only one year when average production per acre for the leading crops was lower than in 1916. The production per acre of ten leading crops averaged about fifteen per cent. smaller in 1916 than in 1915.

The potato crop of 1916 was only 285,000,000 bushels, as compared with an average of 361,000,000 bushels for the previous six years; notable shortages also occurred in the wheat, corn, beans, and onion crops; the cabbage crop was nearly a complete failure. Fortunately, the rice crop was enormous, which accounts for the low price of that commodity, and its resulting popularity. Sweet potatoes were also produced in greater abundance. The amount of live stock marketed in 1916 was greater than usual, which explains why meat prices have not advanced abnormally. Unfortunately, adverse weather conditions in the South during the early part of 1917 blasted the hopes that truck crops from that region might alleviate the situation.

Since potatoes have jumped in price so phenomenally, and since they have become, next to the war, the commonest subject of conversation, they deserve a further word. The acreage was five per cent. less in 1916 than in 1915, but the production per acre was only 80.4 bushels as compared with 96.3 the previous year, a decline of over 15 per cent. The principal potato States are along the northern border of the country; Maine's crop was about the same as in 1915, but Michigan's fell from 21,000,000 bushels to 15,000,000; Wisconsin's from 26,000,000 to 13,000,000; and Minnesota's from 30,000,000 to 16,000,000. The total production of po-

tatoes in 1916 was the smallest it had been since 1908. The banner year was 1912, when this country produced 420,000,000 bushels, as compared with only 285,000,000 in 1916.

Furthermore, the quantity of potatoes left in growers' and dealers' hands in nineteen Northern States on January 1, 1917, as estimated by the United States Department of Agriculture, was only 60,000,000 bushels, or 35 per cent. of the crop, as compared with 106,000,000 bushels on January 1, 1916, or 45 per cent. of that year's crop. In fact the holdings on January 1, 1916, were less than half of the average January holdings for the previous five years. It is interesting to note that 75 per cent. of the holdings were in the hands of the growers themselves, and only 25 per cent. in the hands of dealers. How long do you suppose those 60,000,000 bushels of January first would have lasted if they had been sold to consumers at say a dollar a bushel,—or even two dollars a bushel? But this brings us to the question of food speculation.

Speculation, which is generally misunderstood, is commonly assigned as one of the principal reasons for the high price of foodstuffs. It seems to be a popular belief that it is a crime for dealers to hold back goods for higher prices. Unfortunately our crops are produced during a relatively short season of the year. It will probably be granted by all that it is desirable to distribute one season's crops as evenly as possible over the succeeding months until the next crops mature. It therefore devolves upon someone to assume the risk, responsibility, and capital outlay, of holding commodities in order to perform this important function. The people who do so naturally hope that prices will go up, rather than down, and they must have fairly strong reasons for believing this will be the case, or else they would not take the trouble and suffer the mental anguish involved.

Whoever holds goods in this way, be he farmer or middleman or consumer, is a speculator. He is running the risk of loss or gain from subsequent price fluctuations. Sometimes he makes a profit, and sometimes he suffers a loss. He suffers a loss more commonly than is generally thought. Year in and year out, it is doubtful if the profits are more than enough to pay for the functions performed.

The distribution of a crop throughout the year is determined by the price level, which in turn is brought about through competition of buyers and sellers who are con-

stantly studying market conditions. If the price is held too high during the fall, the crop is not used up fast enough, and the "market breaks" during the following winter or spring. This often happens. If the price is put too low in the Fall, too much of the year's supply is exhausted, and the price soars during the next Spring. This is what happened to potatoes this past year. Although prices were high during the Fall of 1916, they were not high enough to prevent a too rapid using up of the supply, and consequently, when the supply was nearly exhausted by February, the price jumped. If the price had been arbitrarily lowered by some outside authority, such as the Government, the small remaining stock would have been used up at once.

From what has been said, it must be clear that speculation, looked at in its true light, is not only an economic necessity, but an economic benefit as well. We should encourage speculation, rather than despise it. It is ludicrous to read in the daily papers that certain dealers are holding back so many million pounds of this or that commodity, as though it were a crime for them to do so. They are really performing an important economic service by so doing.

Speculation takes different forms in different trades. In the case of grains and cotton, it takes the form of buying and selling for future delivery. This not only brings about the most perfect distribution of a commodity throughout the year, but furnishes a means whereby the actual merchandisers or holders of these commodities can largely avoid the risk of price fluctuations. For example, a terminal elevator company buys wheat in the fall, and immediately sells it to a flour miller for delivery the following May at an advance of six cents a bushel over the price paid. Since the elevator company knows that it will cost only four cents to "carry" the grain until May, it is sure of a profit of two cents a bushel, and need not worry. The flour mill, having bought the wheat at a price for May delivery, knows what price to charge for flour which it contracts to deliver in June. Although dealing in futures is attended by certain evils, this form of speculation has economic advantages which far outweigh the evils, and results in a lower marketing cost, and lower price to the consumer.

Speculation in eggs takes the form of buying them up and putting them in cold storage, trusting that the price will go up, rather than down. The cold-storage companies

do not buy eggs; they merely furnish warehouses, and rent space to the hundreds of dealers, who are the "speculators." The cold-storage company has no control over either the price or the length of time the goods are held in storage. The egg speculators perform an exceedingly important service; reliable statistics show that they lose money during many seasons, and that in the long run they make no more than they are entitled to. As a result of their operations, perfectly wholesome eggs are available at reasonable prices throughout the winter when the hens refuse to lay.

The only danger in connection with speculation is the possibility that some individual may "corner" the market, or that a small number of dealers may get control of the supply, and conspire to lift prices above the level necessary to make the commodities last out until the next crop year. This has been known to happen to a certain extent in the wheat and cotton markets, but really successful corners have been very rare, and have had more or less temporary effects. For most farm products, cornering the market is extremely difficult. Potatoes, for example, are raised over such a wide territory, and by so many individual farmers (many of whom do their own "speculating"), that it is practically impossible for any small group of dealers to get control of a sufficient quantity to artificially affect the price. The mere fact of high prices is no proof of monopoly. Although the Government should keep a constant lookout for manipulation, and for other evils of speculation, it is a significant fact that investigations made during the early part of 1917 have been unable to unearth any conspiracies to artificially raise the prices of foodstuffs, except possibly in the case of onions, though it remains to be seen whether the Government really has a case against the onion dealers who were indicted.

Another popular fallacy exists with regard to our whole marketing organization, which is commonly blamed for high prices, and which is declared by many to be cumbersome and wasteful in the extreme. It is urged that farm products pass through the hands of too many middlemen, and that what is needed is a more direct route from producer to consumer. This is so commonly believed that it is accepted as axiomatic, and it is the foundation rock on which most of the schemes for market reform are built; furthermore, one who attempts to defend the present system runs the risk of being branded a hopeless reactionary and an impracticable

theorist. And yet it would seem strange if, in all our industrial and commercial development of the past half-century—which is supposed to have reached a fairly high state of efficiency—this important part of our economic machinery should have remained so disgracefully inefficient and hopelessly primitive as is commonly assumed.

In the marketing of farm products, certain necessary services have to be performed, and someone has to perform them. In the first place the small and heterogeneous contributions of individual farmers have to be collected for shipment at a country point. They have to be graded, and packed, and held for shipment in car-load lots. Then they are transported hundreds, frequently thousands, of miles,—usually in refrigerator cars. They arrive in the large cities often in train-loads, the quantity fluctuating from day to day, and each car-load often composed of a variety of qualities, sizes, and degrees of ripeness. The fact that many commodities mature first in one section of the country and then in another adds to the complications.

After arrival in the large cities, they have to be cared for in stores and warehouses, broken up into smaller and smaller lots, steered into the thousands of retail channels, and finally passed on to the hundreds of thousands of consumers in half-dozen or half-pound lots. During all this process large amounts of capital are tied up, and credit has to be given; risks of loss are incurred from deterioration of commodities; salesmen have to make business connections and find out just what quality and size of article is desired by each purchaser; delivery equipment has to be maintained for the physical transportation of the goods from jobber to retailer, and from retailer to consumer; and forces of clerks and accountants have to be maintained to keep track of myriads of transactions.

To perform these functions, middlemen have appeared. Country shippers, grain elevators, potato warehouses, collect from the individual farmers and ship in car-load lots to wholesale receivers or commission merchants; this latter class sometimes sells direct to the retail trade, but more commonly to jobbers. The wholesale receiver assembles the goods from all parts of the country, provides storage room for them, roughly sorts them out according to quality, and finances country shippers on the one hand and jobbers on the other. The jobber seeks the retailer with his salesman,

splits up the goods into small quantities, sorts them out according to quality, delivers from day to day, and even from hour to hour, and performs the unsatisfactory task of giving credit to and making collections from retailers.

The foregoing description outlines the usual channels of trade through which farm products pass on their way from producer to consumer. Sometimes an additional middleman appears in the form of a broker, who represents the distant shipper in finding a wholesaler who can handle the goods; or sometimes an auction company appears between receiver and jobber; and sometimes a cold-storage house enters as an additional middleman. But the commonest route is producer, country shipper, railroad, wholesale receiver or commission merchant, jobber, retailer, consumer,—five intermediaries between producer and consumer, counting the railroad, or four intermediaries who are regular dealers in farm produce.

Who is qualified to conclude that there are too many steps between producer and consumer? Is it not possible that there are very good reasons for the development of the present system? Dispassionate investigations of the marketing process yield conclusions which are very different from those assumed by the market "reformers" and by the public at large.

In the first place, it is found that many commodities which pass through the hands of a large number of middlemen are marketed on very small margins, or "spreads," between producer and consumer, and that an additional middleman does not appear unless he can perform certain services, by specializing on them, more cheaply and more efficiently than anyone else. The marketing system is not a hard-and-fast one; it is not made up of fixed and arbitrary divisions of functions between successive middlemen. There is constant experimentation and change going on all the time, as the result of keen competition. Sometimes a dealer assumes the performance of more services than he performed before, and thereby "eliminates" the middleman either preceding him or following him; sometimes, on the other hand, he narrows his functions, and becomes more of a specialist, often increasing the number of middlemen.

Numerous cases might be cited wherein an additional middleman appears for the simple reason that he expedites and economizes the marketing process. The auction company

in the fruit trade is a case in point; likewise the broker; even the co-operative shipping association formed by farmers is an additional middleman, when it performs for the farmers collectively what they were formerly doing individually. If the jobbers of a large city should form a co-operative delivery company, so as to do away with duplication of effort and equipment, economies might possibly result,—but this would be through the addition of another middleman!

In fact the organization of the marketing process is merely an illustration of a fundamental economic law, viz., that division of labor or specialization results in the greatest production of commodities or services for the least effort. From the standpoint of economics, marketing is a part of the productive process. Getting goods from one place to another, and into the hands of those who need them most, is just as necessary as the growing of the commodities in the first place,—and in many cases is much more difficult and costly to perform.

And so we see that by attacking this problem from two different directions—one from a study of actual marketing methods, and the other from the standpoint of recognized economic principles—we come to the same conclusion, viz., that there is ample justification for the present organization of the marketing process, and that it has developed for the simple reason that it performs the marketing service more economically than any other system that has been devised. This does not mean that the present system is perfect by any means. But it does mean that it is unsafe to conclude offhand that there are too many middlemen; in some trades perhaps there are, but in other trades it is possible that economies might be effected by adding another middleman.

If this reasoning is sound, it follows that all revolutionary proposals for the reform of the marketing system based on the assumption that producer and consumer must be brought closer together, are fanciful and uneconomic, and have very little chance of success.

L. D. H. WELD.